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TENTH ANNUAL MEETING,

OHIO STATE BOARD OF COMMERCE

COLUMBUS, JANUARY 7 and 8, 1904.

Advantages to be Derived from a Revision of Business Corporation Laws under the Single Liability Amendment to the Constitution.

BY

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PUBLISHED BY THE
OHIO STATE BOARD OF COMMERCE,
COLUMBUS,
1904.

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ADVANTAGES TO BE DERIVED FROM A REVISION OF BUSINESS CORPORATION LAWS UNDER THE SINGLE LIABILITY AMENDMENT TO THE CONSTITUTION.

BY HON. SMITH W. BENNETT, SPECIAL COUNSEL TO THE ATTORNEY GENERAL.

A radical amendment to the Constitution of Ohio has taken the place of that which existed in that instrument as Section 3 of Article XIII, commonly known as the section prescribing the double liability attaching to stock in Ohio corporations. It is as follows:

"Dues from private corporations shall be secured by such means as may be prescribed by law, but in no case shall any stockholder be individually liable otherwise than for the unpaid stock owned by him or her."

It may be agreed that the overwhelming vote polled for the recent amendment, is an evidence of a widespread demand for a change of policy toward stockholders in domestic private corporations.

Why was this amendment adopted? What purpose was sought to be achieved by its adoption? And does the mere repeal of the double liability provision ensure to corporate organizations sufficient liberaity of

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treatment to encourage the organization of domestic concerns as distinguished from those of other states? An answer to these questions may be helpful in determining what, if any, change should be made in the corporation code.

PURPOSE OF THE AMENDMENT.

Attempting to answer the first query, I contend that the adoption of the amendment was not alone for the purpose of relieving stockholders from the greater liability for future corporate indebtedness, and to remove from the fundamental law that bar to encouraging incorporations at home in preference to foreign states, but to inaugurate means which would serve as an invitation for foreign capital to incorporate with us, and remain with us. Two policies were evident:

(1) To encourage home capital to be invested in domestic concerns.

(2) To invite foreign capital to incorporate in our State.

MEANS FOR SECURING CORPORATE INDEBTEDNESS AMPLE.

If the purpose of adopting the amendment was to take from the General Assembly the power to compel private corporations to secure in some manner their obligations, it failed in such object; for the power conferred by the amendment leaves to the General Assembly, by express language of the amendment, full control of the subject of providing legislative means of securing corporate indebtedness, leaving to the Legislature the choice of any of the many means for that

purpose, save one, viz., that of compelling the stockholders to bear a greater liability than the amount which remains unpaid upon their stock. It should be observed, then, that there is still a field for legislative exploration, in all directions and by all means, save in the one exception noted.

I was not one of those who thought the new amendment to the Constitution was the most perfect that could be devised. It is not contained in the fundamental law of the most progressive states, but is almost an exact reprint of Section 8 of Article XIV of the Constitution of Alabama, and of Section 17 of Article XI of the Constitution of Idaho. My personal view is that dues from private corporations is not a proper subject to be contained in a constitution. It is a matter that is within legislative power, independent of any special constitutional grant, and could be safely trusted to legislative wisdom, without constitutional restrictions. Such is the method adopted in twenty-one of the States, among which we find many of those which are most advanced in corporate legislation.

OHIO SHOULD CREATE A STANDARD OF INTEGRITY FOR THE INCORPORATION OF BUSINESS ORGANIZATIONS.

And here we should be understood as not seeking to authorize the creation of corporations with dishonest purposes, or upon so low plane of responsibility as now exist in several states. The standard must be of the highest, and the public must be protected against concerns organized for speculative purposes. Already, the alarm has been sounded against corporations with

meager assets coupled with gigantic capitalization. Mr. James B. Dill, of New York, of whom it may be said no one has commanded greater attention, or had wider experience, as an attorney in corporate affairs, recently said, in a public utterance:

"Corporations strong in the integrity of their organization, their management and their finances, are to-day forced by their surroundings, compelled by pressure of business competition and obliged by the force of a growing and enlightened public opinion, to draw a line of clear demarkation between themselves and other corporations differently situated—those who cannot stand the test."

If the general impression has gone abroad, that corporations created under the laws of certain states are permitted to defraud the investing public under sanction of law, Ohio must avoid the very appearance of an approach to such standard, and create a high-class corporate law against which such criticism could not be hurled, and the class of corporations, for which Mr. Dill speaks, would voluntarily come under such a law and thus assure the public they can stand the test.

But, we contend, that in return the State should grant to the corporation immunity from other details, which hamper their growth without in any degree compelling corporate honesty.

AN OHIO POLICY OF CORPORATE ENCOURAGEMENT.

To return to the object of the adoption of the Amendment. If the single object alone existed in the mind of the General Assembly, to stop with abol-

ishing the double liability, few changes would be needed in the statute law to accomplish it, such as repealing Sections 3258 and 3260, Revised Statutes, which establish by legislative act that which the constitutional provision had demanded, and the means for the enforcement and collection of the liability thus established. But if the wider policy was the true reason for the adoption of the Amendment, and if Ohio is really seeking to enter upon a campaign of corporate encouragement, many features of the statute law must be removed which serve as serious hindrances in the carrying out of such policy. The latter reason was certainly a controlling one in the consideration of the new Amendment, for almost concurrent with the submission of the Amendment was the enactment of "The Willis Law," and other measures, providing for the raising of a large portion of the state's revenues by an increased tax on corporations. Largely by reason of the income from this form of taxation, it was made possible for the state authorities to reduce the state levy from 2.96 mills to 1.35 mills. And any policy which would increase the number of those corporations, or their amount of capital stock, would, *pro tanto,* serve to further decrease the state levy, and relieve the real and personal property of the State from taxation.

The tax levied upon corporations in this State is not a deterring force against incorporating here, for the fact is plainly apparent that corporations will pay virtually the same tax to the State of New Jersey, as well as the amount imposed in this State, if they are

but permitted to do business under a charter granting them the immunities allowed under New Jersey law.

INCORPORATION SHOULD BE AUTHORIZED FOR MANY PURPOSES.

(1) The Supreme Court holds that the word "purpose" used in Section 3235, Revised Statutes, must be construed in the singular number, and that thereby a corporation can only organize in Ohio for a single purpose, unless express legislative sanction is given. (State ex. rel. v. Taylor; 55 O. S. 61.)

By Act of May 6, 1902, (95 O. L., 391), the General Assembly authorized street railroad companies to purchase the property, franchises and privileges of an electric light, natural, or artificial gas company, organized to sell gas or electricity for power, light, heat or fuel purposes, and to have all the rights and powers of the companies whose property and franchises are purchased. This method of procedure combines five distinct purposes in one company. If this legislation is thought to be good public policy, why require that the object be accomplished in such an indirect way? Why not directly, by act, authorize the incorporation of a company for mnay purposes, instead of one? This could be accomplished in the manner provided by the statute of New Jersey, which, in substance, reads:

"Three or more persons may become a corporation for any lawful purpose *or purposes* whatever other than a savings bank, building and loan association"—and other special forms of corporations.

(2) The General Assembly, sooner or later, must seriously consider the evil of certain states, granting powers to corporations organized under their law to do and perform certain things without the state of their creation *which they are not authorized to do or perform within such state.*

As an illustration: By Section 6 of the General Corporation Laws of New Jersey, (Laws of 1896, Ch. 185), after denying the right to incorporate banks, building and loan associations, insurance, surety, railroad, telegraph, telephone, and certain other companies under the general incorporation laws of that state to do such business in that state, it further provides that,

"It shall, however, be lawful to form a company hereunder for the purpose of constructing, maintaining and operating railroads, telephone or telegraph lines *outside of this state.*"

By this policy two classes of corporations are permitted: Those authorized to do business within the state and elsewhere; and those which are only permitted to do business outside the state. New Jersey is not the only state creating such corporations. There is a profit in it, hence many are engaged in doing the same thing. The question of whether it is right—in an interstate sense—does not enter into the consideration of those creating them. Common honesty would seem to require that where they are shorn of power in the state of their creation, they should equally be

devoid of power in any other state. But, waiving the moral side of the argument, let us inquire what shall be the policy of Ohio toward such corporations. The power of the General Assembly is full and ample to correct the wrong. It is left entirely in the hands of each individual state to forbid the right of such corporations to enter the state. The comity existing between states, to permit the concerns of other states to do business therein, can be withdrawn, and should be, when it works an injury to the state permitting it.

Shall Ohio deny to a corporation the privilege of exercising any power *in Ohio* which the corporation is denied in the state of its creation, or shall this state enter into the field of creating corporations with similar powers? Or shall it continue the same policy toward such corporation, of allowing them, unchallenged, to exercise every right conferred in the foreign charter?

As evidence of a legislative policy of favoring foreign as against domestic corporations, I cite Section 148d, Revised Statutes, where it is provided that the Secretary of State shall determine, and thereupon issue a certificate to such foreign corporation that it "has complied with all the requirements of law to authorize it to do business in this state, and that the business of the corporation to be carried on in this state is such that can be lawfully carried on by a corporation incorporated under the laws of this state for *such or similar business, or if more than one kind of business, by two or more corporations so incorporated for such kind of business exclusively.*" Thereby grant-

ing powers to a foreign corporation to do in Ohio, what it would take two or more domestic corporations to do.

REMEDIES FOR VIOLATIONS OF INTERSTATE COMITY.

Regarding the remedies: We can repeal all the laws giving superior advantages to foreign over domestic corporations. We can retaliate by creating corporations authorized to exercise powers outside of Ohio, that from a standpoint of policy we would not permit to be done in Ohio. We can discriminate in favor of domestic and against foreign corporations in the amount of the franchise tax charged annually.

A DISCRIMINATING TAX.

I favor the discrimination in the tax. As this form of taxation is not by the Constitution, required to be uniform, even among domestic corporations, so a different percentage may be levied upon a foreign corporation than upon a domestic one, so long as it is not made a charge upon interstate commerce. No one can give a satisfactory reason, why a foreign corporation, should have superior rights in Ohio, over a domestic, and only pay the same amount of tax. They should either be reduced to a level as to powers, or the greater powers should demand a greater tax.

One result would naturally follow such a plan. Ohio could thus call home all her corporate capital elsewhere incorporated, and by reason of the differential in the tax, induce foreign corporations now doing business here, to reincorporate in Ohio.

RESIDENT AGENT, BUT NOT RESIDENT DIRECTORATE SHOULD BE REQUIRED.

(3) It is evident that the policy in force in Ohio, by which a corporation must have at least five directors, a majority of whom must reside within the state of Ohio, should be modified if we seek by appropriate legislation to induce non-residents of the state of Ohio to incorporate their business concerns here. Many of the states require no resident directors of the corporations incorporated in such states, and some of them require but one.

I should think it would be a safe, conservative policy, to authorize a corporation composed of non-residents of the state of Ohio, to be incorporated here, without maintaining a resident directorate, but the protection of its citizens and investors in such corporations, and the right of action in its local courts could be fully protected, as in West Virginia, New Jersey and elsewhere, by requiring such corporation to maintain an office and an agent within the state of Ohio, where the stock and transfer books should always be kept. The present policy, as evidenced by our statute law, will continue to keep foreign capital from incorporating here.

The agent of such corporation should be required to be a citizen of the state of Ohio, and it might be provided that a domestic corporation, authorized so to act by appropriate legislation, could become such agent. This would open a great field for the trust companies of the state, which would most probably

require the enlargement of Section 3821a of the Revised Statutes to permit such agency business to be done.

CORPORATIONS SHOULD BE AUTHORIZED TO REGULATE EXAMINATION OF BOOKS BY STOCKHOLDERS.

(4) Regarding the books of the corporation—meaning the books other than the register and transfer book of stock—should be left in charge of the directors of the corporation; and I contend Section 3253, Revised Statutes, ought to be so amended as to authorize a corporation to adopt regulations regarding the examination of its books.

As the statute now reads governing this privilege, and as construed by the courts, a stockholder, no matter how small his holdings, may demand an inspection and examination of the books of the corporation and thereby become possessed of its secrets; and if such inspection is refused by the directors, or those having charge of the books, such stockholder may bring his action in a Court of Common Pleas, and secure equitable aid to compel the officers of the corporation to grant him such inspection. And the courts have held that it is mandatory to award such relief, and the question of the motive of such stockholder in demanding such examination, is not an issue to be determined in the case.

It should be admitted that a stockholder has the right of examination under certain circumstances. But this should be dependent upon some specific duty due to the stockholder; and upon an allegation of

fraud against those rights or in derogation of them, such inspection should be compelled to be given by a court.

Permit a corporation by its regulations to provide when, and under what circumstances, an inspection shall be given, and it could thus be left to the stockholder to protect himself, and if the clause be objectionable to him, he certainly has the privilege of refusing to invest in a corporation having any objectionable by-laws and regulations. The possible injustice arising from the operation of such a section, would be small as compared with the power given to rival concerns of prying into the private accounts and business of the company by having a few shares of its stock purchased, and using the power, now granted for that purpose.

REVISION OF BUSINESS CORPORATION LAWS SHOULD HAVE SERIOUS CONSIDERATION.

It is not the purpose of this paper to attempt in even the most general way to summarize some of the objections now existing to the present chapter of statutory law governing corporations. That is properly the work of a legislative committee or commission, but it is apparent that, in view of that policy which has heretofore hindered and deterred corporations from organizing with us, and has re-acted against the welfare of the state, that serious consideration should be given to this subject. It is not a large subject, such as the enactment of a civil, municipal or school code, for the general corporation law could be

abridged, and that probably within forty sections. But in addition to that we have about twenty chapters covering special classes of corporations, that for the purposes advocated here would not need to be touched. This work could be done at the present session of the General Assembly and would result in much good to the state.

COLUMBUS, OHIO:
SPAHR & GLENN, PRINTERS.
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